ARTHUR ANDERSEN

NOTE –
IT IS UNCLEAR WHY CHASE RECEIVED THIS LETTER OR WHY THEY SENT IT TO ENRON

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September 29, 1999

Chase Securities Inc.
270 Park Avenue
New York, NY 10017

Dear Sir or Madam:

We have been engaged to report on the appropriate application of United States generally accepted accounting principles (US GAAP) to the hypothetical transaction described below. This report is being issued to Chase Securities Inc. for assistance in evaluating accounting principles for the described hypothetical transaction. Our engagement has been conducted in accordance with standards established by the American Institute of Certified Public Accountants.

Hypothetical Transaction:

1. Sponsor, a U.S. corporation has two wholly owned domestic corporate subsidiaries ("Sponsor Sub 1" and "Sponsor Sub 2"). Sponsor Sub 1, Sponsor Sub 2, and an unrelated third party investor (the "Investor") will form a partnership (the "Partnership"). The Partnership will be organized as a limited partnership under the Delaware Revised Uniform Limited Partnership Act.[1] Sponsor Sub 1 will be its general partner. Sponsor Sub 2 and the Investor will be its limited partners.

2. Sponsor Sub 1 will purchase $500 million of Sponsor common stock (the "Sponsor Common Stock") in the marketplace. Sponsor Sub 1 will contribute the Sponsor Common Stock to the Partnership in exchange for 97.0 percent of the Partnership's common interests (in the form of GP and LP units). Common Interests for purposes of this memo is defined as a partner's entitlement to profits or losses after the preferred return has been allocated. Sponsor Sub 2 will contribute intangibles (the "Property") with a tax basis of -0- and a fair market value of $500 million in exchange for 1.5 percent of the common LP units and a preferred LP interest that entitles Sponsor Sub 2 to an 8 percent preferred return on $500 million of its contribution. As the common interest holders, Sponsor Sub 1 and Sponsor Sub 2 (and

[1] It should also be possible for the Partnership to be organized as a limited liability company.

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Investor) will, for US Federal Income Tax (FIT) purposes, be allocated all remaining profits and losses (including book gains and losses that may arise upon a distribution or revaluation of Partnership property), after allocation of the preferred returns, pro rata in accordance with their common interest holdings.

3. The Investor will contribute $500 million in cash in exchange for 1.5 percent of the common LP interests and a preferred LP interest that entitles the Investor to an 8 percent preferred return on its contribution. The Partnership will be permitted to invest the $500 million in cash contributed to it by the Investor in certain permitted investments. Furthermore, the Partnership will lease the contributed Property to the Sponsor or a Sponsor affiliate for a period of years.

4. The following sets forth the FIT assumptions and analysis:

   a. The Property contributed by Sponsor Sub 2 would be amortizable over 15-years if newly purchased by the Partnership.

   b. The Partnership will adopt the remedial method under Treas. Reg. § 1.704-3.

   c. The taxable income allocated to Sponsor Sub 2 should exceed the Section 704(b) book income allocated to such Partner by the amount of section 704(b) book amortization with respect to the contributed Property.

   d. Assuming Sponsor Sub 2 receives a cash distribution annually equal to its preferred return, it's tax basis in its Partnership interest should increase each year by the excess of taxable income over section 704(b) book income allocated to such partner.

   e. If Sponsor Sub 2 were to receive a distribution of the Property in liquidation of its interest in the Partnership, it should take a basis equal to its then existing outside tax basis in its Partnership interest.

   f. Sponsor Sub 1 should be able to receive a liquidating distribution of the Sponsor Common Stock without recognizing gain for FIT purposes. Sponsor Sub 1 should take a substituted basis in such property it receives from the Partnership in liquidation of its interest.

   g. With respect to the property which Sponsor Sub 1 receives in liquidation of its interest, Sponsor Sub 1 should be able to undertake steps to permanently eliminate any deferred FIT gain inherent in such property.

h. For purposes of this memorandum we will assume the investor will receive upon retirement from the Partnership an amount equal to its original contribution in cash. As such it can be assumed that the tax consequences to the investor associated with its residual share of income are deminimus.

Accounting Discussion:

You have asked us to address the accounting for this transaction under US GAAP in the consolidated financial statements of Sponsor. We have not been asked to address and, accordingly have not addressed, the treatment of this transaction for FIT purposes, regulatory purposes or any purposes other than treatment under US GAAP and all references to the treatment for FIT purposes are based on your analysis as described above. Accordingly, we express no opinion on the FIT consequences the transaction.

Accounting for Sponsor Sub 1, Sponsor Sub 2, and the Partnership

The rules for consolidation of subsidiaries are set forth in Accounting Research Bulletin No. 51 (ARB 51), Opinion No. 18 of the Accounting Principles Board (APB 18) and Statement No. 94 of the Financial Accounting Standards Board (SFAS 94). These rules specify that a company should generally consolidate the accounts of an investee when it has a controlling financial interest in the investee. The usual condition for a controlling financial interest is ownership of a majority voting interest. An interpretation issued by the American Institute of Certified Public Accountants generally extends the conclusions of APB 18 to partnerships. Accordingly, Sponsor would consolidate Sponsor Sub 1, Sponsor Sub 2 and the Partnership (which it controls as general partner).

Under US GAAP, the non-affiliate equity holders of a consolidated investee are treated as minority interests in the consolidated financial statements. Hence, Investor's investment in Partnership would be reflected as a minority interest in Sponsor's consolidated financial statements.

The Financial Accounting Standards Board (FASB) has issued an Exposure Draft (the ED) that would significantly revise the accounting rules for consolidated financial statements. As presently proposed, we do not believe that the ED would change our conclusions regarding the consolidation of Sponsor Sub 1, Sponsor Sub 2 or of Partnership by Sponsor.

Accordingly, all transactions among Sponsor, Sponsor Sub 1, Sponsor Sub 2 and the Partnership would eliminate in consolidation.

Purchase of the Sponsor Shares in the Market

Since Sponsor Sub 1 is a wholly-owned subsidiary of Sponsor, its purchase of the Sponsor common shares in the market place will be recorded as a purchase of treasury shares in Sponsor's consolidated financial statements (i.e. will reduce consolidated equity). The transfer of these shares to Partnership will not change this accounting since Partnership is also a consolidated entity.

Business combinations that meet all of the criteria to be accounted for using the pooling-of-interests method in accordance with APB 16 must use this method. Otherwise, APB 16 requires the use of the purchase method. Among the criteria for a pooling, are i) there must be no alterations of the equity interests of the combining companies in contemplation of the business combination and ii) the combining companies may not have aggregate tainted treasury stock, as defined, in excess of 10% of the shares being issued to effect the business combination. With certain exceptions, treasury stock that is purchased within two years preceding the date a plan of combination that is to be accounted for as a pooling is initiated, is considered to be so called "tainted treasury stock" for purposes of applying this rule (Paragraph 47d of APB 16). The shares being purchased by Sponsor Sub 1 would likely be tainted treasury shares for these purposes.

To the extent that treasury shares reacquired within two years prior to initiation or between initiation and consummation of a pooling transaction have not been reissued or specifically reserved, an equivalent number of shares of treasury stock may be sold prior to consummation to an independent party to "cure" the presumed violation of paragraph 47d. The SEC staff agrees that so long as the treasury shares were acquired for a business purpose other than to circumvent a pooling-of-interests criterion, issuance of shares to cure the taint may occur at any time prior to consummation. Although the issuance of shares is a change in equity interest, the reissuance of the shares in the market is not a transaction that is preferential to any one shareholder group. Therefore, the taint may be cured by issuing the shares for fair value to an independent third party (assuming fair value can be established) or into the market at any time prior to consummation without violating the pooling-of-interests requirements.

The FASB has issued an exposure draft that comprehensively reconsiders the accounting standards for business combinations. This exposure draft proposes to eliminate the pooling of interests method and thus the concept of tainted treasury shares. The proposed exposure draft would be effective for transactions initiated after the issuance of a final statement (the effective date is anticipated to approximate January 1, 2001 for calendar companies). There is no way to predict whether or when this exposure draft will be adopted or what changes, if any, may be made to its provisions.

Investment by Investor

Investor's cash contribution would be recorded as a minority interest in Sponsor's consolidated financial statements. Investor would be allocated its 8% preferred dividend plus 1.5% of Partnership's net income after all preferred returns (including the preferred return to Sponsor Sub 2). These amounts would be charged against Sponsor's consolidated income statement as minority interest in earnings.

Accounting For Income Taxes

Accounting for income taxes is governed by SFAS No. 109. That Statement provides that, among other things, assets and liabilities which are recorded at different amounts for financial reporting purposes than for income tax purposes create basis differences for which a deferred tax asset or liability might be required. You have informed us that, in the transaction discussed herein, Sponsor Sub 2's tax basis in its preferred LP units will increase each year by approximately $33 until such time as Sponsor Sub 2 has a $500 basis in its preferred LP units, while Sponsor Sub 1's tax basis in its common Partnership units decreases from $500 to $0 over the life of the transaction. The resultant current tax charge and tax benefits will approximately offset in Sponsor's FIT return. Further, you have informed us that the Property can either be distributed in year 15 with its tax basis stepped up to $500 or can be distributed in any given year and be stepped up approximately by an amount equal to the product of (i) $33 and (ii) the number of tax years which have elapsed since the formation of the Partnership. Furthermore, you have informed us that the Sponsor common stock can be withdrawn from the Partnership and retired without ever resulting in a taxable gain.

SFAS No. 109 provides that deferred taxes be provided only for basis differences which qualify as temporary differences, meaning those differences between the tax basis of an asset or liability and its reported amount in the financial statements that will result in taxable or deductible amounts in future years when the book carrying value of the asset or liability is recovered or settled, respectively. Further, deferred tax assets or liabilities are recorded only by the specific entity on whose books such differences reside. In other words, since the Partnership is a true tax "flow through" entity (i.e., not a taxpayer), no deferred tax asset would be provided on the books of the Partnership itself.

As the FIT dynamics of this transaction create tax basis each year available to Sponsor's consolidated group through the increase in the tax basis of Sponsor Sub 2's preferred LP units, without such an increase for financial reporting purposes, the tax effect of the increase in basis each year would be recorded as an asset (or as a decrease to net deferred tax liability) each year with a corresponding credit to income tax expense in Sponsor's consolidated financial statements (subject to a net realization test if there is a net deferred tax asset). Further, you have informed us that Sponsor has available to it a planning strategy which, without the incurring of substantial cost, would enable it to transfer the common shares to Sponsor and retire them without incurring a tax cost. Accordingly, the decline in the tax basis of the Sponsor Sub 1's Partnership interests each year does not result in a temporary difference that would require a charge to tax expense.

Other

In situations such as these, in which the ultimate realization of the economic and financial statement benefits is dependent upon certain positions that will be taken on current and future tax returns, we believe that the financial statement benefits should be recorded only if it is probable that the pertinent tax positions will be sustained. The term "probable" is discussed in SFAS 5, *Accounting for Contingencies,* but is not numerically defined therein or elsewhere in the authoritative accounting literature. It is clear that it requires a higher degree of likelihood than the "more likely than not" standard discussed in SFAS 109 (which represents a threshold of more than 50%).

The ultimate responsibility for the decision on the appropriate application of generally accepted accounting principles for an actual transaction rests with the preparers of financial statements, who should consult with their continuing accountants. Our judgment on the appropriate application of generally accepted accounting principles for the described hypothetical transaction is based solely on the facts provided to us as described above; should these facts and circumstances differ, our conclusion may change. We have not been asked to address and have not addressed any tax matters relating to this transaction.

Our opinion is as of the date of this letter and we do not assume an obligation to update this opinion for subsequent changes in relevant rules or practice.

Very truly yours,

Arthur Andersen LLP

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